IN THE

Supreme Court of the United States

OCTOBER TERM, 1978

No. 78-1208

CURTIS CIRCULATION COMPANY,

Petitioner,

vs.

GOULD PAPER CORPORATION,

Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

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PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

The petitioner Curtis Circulation Company respectfully prays that a writ of certiorari issue to review the judgment and opinion of the United States Court of Appeals for the Second Circuit entered in this proceeding on December 13, 1978.

Opinions Below

The opinion of the Court of Appeals, not yet reported, appears in Appendix A hereto. The opinions of the District Court for the Southern District of New York, all unreported, are set forth in Appendices B, C and D, respectively.

Jurisdiction

The judgment of the Court of Appeals for the Second Circuit was entered on December 13, 1978. A timely motion for a stay of the mandate was granted on January 9, 1979, and this petition for certiorari was filed within 30 days of that date. This Court's jurisdiction is invoked under 28 U.S.C. § 1254(1).

Questions Presented

1. Whether in an action on an assignment the account-debtor can assert as a defense the assignee's overcharges to the assignor so as to prove the absence of a debt to which the assignment could apply.

2. Whether in violation of the provisions of the Federal Rules of Civil Procedure a Court should permit a plaintiff to cure its failure of proof, absent surprise, excusable neglect or newly-discovered evidence, by reopening the record for additional testimony.

Statutory Provision Involved

New York Uniform Commercial Code § 9-318(1).

Unless an account-debtor has made an enforceable agreement not to assert defenses or claims arising out of a

sale as provided in Section 9-206 the rights of an assignee are subject to:

(a) all the terms of the contract between the account-debtor and assignor and any defense or claim arising therefrom; and

(b) any other defense or claim of the account-debtor against the assignor which accrues before the account-debtor receives notification of the assignment.

Statement of the Case

This action was commenced by Gould Paper Corporation ("Gould") to recover damages against Curtis Circulation Company ("Curtis"), the petitioner herein, pursuant to a limited security assignment (Appendix E). The assignment reserved for Gould as security for paper it sold to Penthouse International, Ltd. ("Penthouse") a portion of the proceeds of a distribution agreement between Penthouse and Curtis, the distributor of Penthouse Magazine. Federal jurisdiction was invoked on the ground of diversity of citizenship.

During the proceedings before the District Court, both Curtis and Penthouse tried unsuccessfully to focus that Court's attention upon the substantial controversy between Penthouse and Gould. For several years, Gould had surreptitiously overcharged Penthouse by almost $2,000,000, which is the subject of a prior commenced, but still unresolved, lawsuit by Penthouse against Gould in the New York state court. However, in bringing a diversity action against Curtis, Gould sought to gain an advantageous procedural posture by pursuing its claim under the assignment against Curtis—a marginal spectator to the long-standing controversy between Penthouse and Gould—and avoiding its overriding dispute with the real party in interest—Penthouse.

The District Court denied Curtis' motion to dismiss for the failure to join an indispensable party, denied Penthouse's motion to intervene and prevented Curtis from litigating the question of overcharges (Appendix B), an issue central and essential to determining the amount of the debt secured by the assignment.

Following a bench trial in early 1977, the District Court in its opinion dated November 2, 1977 (Appendix C) upheld the validity of the assignment and awarded Gould $717,786.33 plus interest and costs. However, while the District Court correctly observed that such was the amount due Gould from Penthouse for paper sold and delivered, it erroneously awarded that full amount against *Curtis*, despite certain inherent limitations in the assignment* which put a ceiling of $88,720.80 upon what Gould could recover from Curtis. But Gould at the trial utterly failed to rebut the limited nature of the assignment and omitted to prove the extent of *any* damages to which it may have been entitled thereunder.

The same day judgment was to be entered, Curtis pointed out to the District Court the fatal deficiencies in Gould's proof. The District Court then decided to reopen the record to receive additional evidence, not merely to show the dates and amounts of payment required to calculate what was due Gould under the assignment, but to permit Gould to recite its subjective opinion as to what the assignment meant when it was drafted almost ten years ago.

* The assignment by its terms is limited to "the initial and first payments" to be made from Curtis to Penthouse under their distribution agreement (See Appendix E). It is undisputed that were this limitation to operate together with the rider to the assignment, Gould's demand under the assignment would capture no more than $88,720.80 since several "initial and first payments" had by that time been properly paid over to Penthouse. See N.Y.U.C.C. § 9-318(3).

The trial resumed on March 20, 1978. The District Court credited Gould's parol testimony and refused to enforce the inherent limitation to "initial and first payments" clearly set forth in the body of the assignment (Appendix E). By its opinion dated June 15, 1978, (Appendix D), the District Court upheld its earlier award to Gould of $717,786.33 plus interest and costs. The Court of Appeals affirmed in an opinion dated and filed December 13, 1978 (Appendix A).

REASONS FOR GRANTING THE WRIT

I.

The decision below conflicts with New York common law and the Uniform Commercial Code.

The decision of the Second Circuit, upholding the District Court's refusal to permit Curtis to raise payment as a defense to Gould's assertion of the assignment, both contradicts existing state law and distorts the meaning of § 9-318(1) of the Uniform Commercial Code, enacted in virtually identical form in 51 jurisdictions.*

Since it is undisputed that Gould never received an absolute assignment, but only an assignment as *security* for the payment of Penthouse's paper bills, it was incumbent upon Gould to first establish the existence of a debt owing from Penthouse before it could recover under the assignment. Penthouse's $2,000,000 claim for overcharges completely eliminates Gould's claim of $717,786.33 for paper sold and delivered. Yet both the District Court and the Second Cir-

* The Uniform Commercial Code, with variations, is law in all states but Louisiana and is also law in the District of Columbia and the Virgin Islands.

cuit barred Curtis from interposing the defense of payment (in this case, overpayment), relying upon § 9-318(1) of the New York Uniform Commercial Code.

That statute, however, does not purport to enumerate *all* of the claims to which an assignee's rights are subject. Even a cursory reading of § 9-318(1) reveals that it does not attempt to deal with an account-debtor's assertion of an assignor's claim against an assignee; instead, § 9-318(1) speaks only to claims between the account-debtor and the assignor, leaving other issues, such as the defense of payment raised in this case, to resolution under the common law. The Uniform Commercial Code itself provides that "[u]nless displaced by the particular provisions of this Act, the principles of law and equity . . . shall supplement its provisions." N.Y. UCC § 1-103 (McKinney's 1964). Since Article 9 of the Code makes no attempt to even treat an account debtor's assertion of the defense of payment under a security assignment, the solution must be found in the common law.

The highest appellate court in New York to consider the issue held that an account debtor could raise the absence of a debt as a valid defense to a security assignment. *Warren* v. *Chemical Bank & Trust Co.*, 76 N.Y.S.2d 366 (Sup. Ct. N.Y. Co. 1947), *rev'd*, 274 App. Div. 785, 79 N.Y.S. 2d 776 (1st Dep't 1948). Similarly, if Curtis had been offered the opportunity to establish the overcharges to Penthouse, and in fact had done so, then that would have eliminated or reduced the debt owing from Penthouse to Gould which Gould has asserted as the basis of enforcing its security assignment.

The concept of "attachment" under § 9-204 of the Code, argued below by Gould and referred to by the Second Circuit, is inapplicable since the appellate court in *Warren* could not, and did not, rely upon a concept which had not

become law in New York until September 27, 1964, the date the Uniform Commercial Code took effect in that jurisdiction. The *Warren* court's holding, which provides the common law supplement to the question not considered by § 9-318, establishes the prevailing New York rule that the account-debtor (Curtis) can deny the existence of a debt from the assignor (Penthouse) to the assignee (Gould) in an action by the latter to enforce a security assignment.

The only authority relied upon by Gould below is *Williams Press, Inc.* v. *Kable News Co.*, 84 M.2d 118, 375 N.Y.S.2d 515 (Sup. Ct. Alb. Co. 1975), a lower court decision which involved an *absolute* assignment rather than a *security* assignment. In that case, the assignment constituted the very "method of payment" by which a publisher was to pay its printer and was specifically made "for payment of the balance of printing costs", 375 N.Y.S.2d at 516, 517, whereas here it is undisputed that Gould's assignment, intended as security only, never governed and was never intended to govern the "method of payment" from Penthouse to Gould. Moreover, that case did not involve the defense of breach of contract between the assignor and the assignee, the court observing that "neither [the distributor] nor [the publisher] have raised any valid defenses to the assignment". 375 N.Y.S.2d at 517.

The Second Circuit's unprecedented decision below conflicts with the authority of the highest state court to consider the issue and distorts the purpose of § 9-318(1) of the Uniform Commercial Code. If left undisturbed, that decision may have nationwide commercial implications in each of the 51 jurisdictions in which the Code has been enacted. These conflicts warrant the grant of certiorari to review the judgment below.

II.

The decision below conflicts with the orderly rules of civil procedure.

The Second Circuit refused to disturb the District Court's exercise of discretion in reopening the record for additional evidence because of "Curtis' failure to raise the damages issue earlier" (Appendix A). Similarly, the District Court "shared" what it perceived to be "a clear misunderstanding as to the issues before the Court" (Appendix D). These conclusions, however, are belied by the proceedings below and the evidence in the case. If a district court is permitted to exercise unfettered discretion to allow additional evidence after the record has been closed and the parties afforded ample opportunity to litigate their respective contentions, the orderly procedure embodied in the Federal Rules will become illusory.

Curtis had consistently argued below that the assignment was limited by its terms to the "initial and first payments" to be made under the distribution agreement between Curtis and Penthouse (see Appendix E) and, therefore, the most that Gould could recover was $88,720.80. Prior to the trial, the Executive Vice-President of Penthouse argued this limitation in an affidavit, which was promptly rebutted by the affidavit of Gould's own President. Moreover, at trial the following exchange occurred during the direct examination of Curtis' witness:

> "Q. Mr. Kreditor, were the second, third or fourth payments made by Curtis to Penthouse subject to the Gould assignment?
>
> A. No.
>
> Q. Ever?
>
> A. Never. To my knowledge, never.
>
> The Court: Was that in the assignment?
>
> Mr. Grutman: Yes, Your Honor.

> The assignment says specifically by its rider that only the first payment is to be the subject of the assignment. Does Your Honor see that? The end of the first full paragraph on the first page which says, 'It is understood and agreed that this assignment shall attach to the initial and first payments to be made thereunder.'
>
> The Court: I see it.
>
> Mr. Rosenfeld: Your Honor, I am not sure what point Mr. Grutman intends to draw from that, but I do think that Your Honor should know that that reading of that sentence is disputed by Gould, was disputed by Gould previously."

Having litigated the issue both before and during the trial, Gould cannot reasonably urge "surprise" as an excuse to justify a reopening of the record. If surprise was a factor in Gould's failure to rebut at trial the limitation of its assignment, it could have sought a continuance to properly prepare its proof. *Melanson Co.* v. *Hupp Corp.*, 391 F.2d 902, 903 (3rd Cir. 1968); *Moylan* v. *Siciliano*, 292 F.2d 704, 705 (9th Cir. 1961). Since Gould had a full opportunity to present its evidence at trial to support proof of damages, but chose not to, it had no excuse which would warrant the extreme and unfair practice of reopening the record. *Mack* v. *Earle N. Jorgenson Co.*, 50 F.R.D. 469, 470 (E.D. Wis. 1970), *aff'd*, 467 F.2d 1177 (7th Cir. 1972); *Bell Telephone Laboratories, Inc.* v. *Hughes Aircraft Co.*, 73 F.R.D. 16 (D. Del. 1976). As Judge Weinfeld recently ruled in *Union Bank of Switzerland* v. *HS Equities, Inc.*, 458 F. Supp. 1166, 1167 (S.D.N.Y. 1978), "absent a compelling excuse a new trial need not be ordered to permit a party to introduce evidence which it had available to it at the time of trial".

By neglecting to prove the damages, if any, to which it was entitled, Gould failed to discharge its burden and was

not entitled to yet another opportunity to prove what it had omitted the first time around. *Cedar Creek Oil & Gas Co.* v. *Fidelity Gas Co.*, 249 F.2d 277, 285 (9th Cir. 1957), *cert. denied*, 356 U.S. 932 (1958); *Butler* v. *Pettigrew*, 409 F.2d 1205, 1207 (7th Cir. 1969); *Cannister Co.* v. *National Can Corp.*, 71 F. Supp. 49, 50 (D. Del. 1946).

Moreover, the silence of the pre-trial order on the issue of the assignment's limitation did not prohibit Curtis from raising the question at trial, particularly in view of Gould's failure to object to this testimony. See *Bucky* v. *Sebo*, 208 F.2d 304 (2d Cir. 1953). In *Pacific Indemnity* v. *Broward County*, 465 F.2d 99 (5th Cir. 1972), the Fifth Circuit described an appeal as presenting "the Case of the Forgotten Issue", *id.* at 100, concluding that the failure to raise an issue in the pre-trial order inures to the detriment of the party with the burden of proof, *id.* at 103, and to require a party to remind its adversary in the pre-trial order of what it was obligated to prove "would strain the logic of our adversarial system and would destroy much of the usefulness of a pre-trial order as a device to reduce and limit the issues at trial", *id.* at 104.

The fact that the District Court may have misapprehended the implications of the assignment's inherent limitation, raised both prior to and during trial, does not constitute the kind of error which should inure to the benefit of Gould, particularly since Gould itself debated the issue in affidavits prior to trial and continued to maintain at trial that the asserted limitation was "disputed".

By permitting Gould to belatedly cure deficiencies in its proof, the District Court violated the orderly rules of evidence and procedure relied upon by Curtis throughout the litigation. While reopening the record after all sides have rested may be permitted upon a proper showing of surprise, it has been generally condemned as a "pernicious practice". *Reconstruction Finance Corp.* v. *Commercial Union etc.*, 123 F. Supp. 748, 750 (S.D.N.Y. 1954).

Review for abuse of discretion "does not mean . . . that an appellate court should automatically confirm such exercise of discretion", but "would be remiss in [its] duties if [it] chose only to rubber stamp such orders of lower courts". *Wilson* v. *Volkswagon of America, Inc.*, 561 F.2d 494, 505-06 and n.30 (4th Cir. 1977), quoting Waterman, *An Appellate Judge's Approach When Reviewing District Court Sanctions Imposed for the Purpose of Insuring Compliance with Pretrial Orders*, 29 F.R.D. 420, 424-25 (1961). By sanctioning the arbitrary abuse of discretion, the Second Circuit has so far departed from the accepted and usual course of federal practice and procedure as to warrant review by this Court.

CONCLUSION

For these reasons, a writ of certiorari should issue to review the judgment and opinion of the Second Circuit.

Dated: February 2, 1979

Respectfully submitted,

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[APPENDICES FOLLOW]

APPENDIX A

Opinion of the United States Court of Appeals for the Second Circuit

(Filed—December 13, 1978)

UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT

At a Stated Term of the United States Court of Appeals, in and for the Second Circuit, held at the United States Courthouse in the City of New York, on the 13th day of December, one thousand nine hundred and seventy-eight.

Present:

HON. WILLIAM H. TIMBERS
HON. THOMAS J. MESKILL
HON. JOHN F. DOOLING, JR.
United States District Judge
Sitting by Designation

78-7333

GOULD PAPER CORPORATION,
Plaintiff-Appellee,

v.

CURTIS CIRCULATION COMPANY,
Defendant-Appellant.

Appendix A

Appeal from the United States District Court for the Southern District of New York.

This cause came on to be heard on the transcript of record from the United States District Court for the Southern District of New York, and was argued by counsel.

On Consideration Whereof, it is now hereby ordered, adjudged, and decreed that the judgment of said District Court be and it hereby is *affirmed* substantially on the opinions of Judge Stewart, supplemented by the following brief statement of our reasons for affirmance.

The appeal is from a judgment, after a bench trial, in amount of $717,786.33, plus interest and costs, in favor of appellee Gould Paper Corporation and against Curtis Circulation Company arising out of an assignment which reserved for Gould as security for paper it sold to Penthouse International, Ltd. the proceeds of a distribution agreement between Penthouse and Curtis, the latter being the distributor of Penthouse Magazine.

The chief issue presented is whether the district court erred in interpreting the assignment to reach all the proceeds of the Curtis distribution agreement and not merely the "on-sale date" portion. Other subordinate claims of error will be referred to below.

Curtis comes to this Court with the burden of showing that Judge Stewart's interpretation of the "initial and first" language of the assignment was clearly erroneous. Fed. R. Civ. P. 52(a). While the construction of an unambiguous contract, and the decision whether a contract is ambiguous, are conclusions of law, the construction of an ambiguous term is a finding of fact. See 4 Williston on Contracts §616, at 652 p. 12.

Appendix A

Appellant has failed to sustain this burden. Its arguments before us basically represent an effort to refight the battle waged below. The decision below in essence, rested on a determination as to what weight and credibility to give the evidence that was heard on the negotiations leading to the disputed language. We are satisfied that Judge Stewart's determination in that regard was correct.

Appellant's claim that it was error not to permit it to assert Penthouse's overcharge and other claims against Gould is without merit. New York's Uniform Commercial Code §9-318 details the claims to which an assignee's rights are subject, in the absence of an agreement not to assert defenses under §9-206; claims of the assignor against the assignee are not among them. *Warren* v. *Chemical Bank & Trust Co.*, 76 N.Y.S.2d 366 (Sup. Ct., N. Y. Co., 1947), *reversed*, 274 A.D.785, 79 N.Y.S.2d 776 (1st Dept. 1948), is not on point. There a key event never took place, i.e., the generation of profits from a specified sale which were to be paid to the assignee. By contrast, the security interest here attached with the paper deliveries to Penthouse from Gould. N.Y. U.C.C. §9-204.

The remaining claims of error warrant only brief mention. The decision whether to reopen the record for additional evidence is committed to the discretion of the trial judge. 6A Moore's Federal Practice ¶59.04[13] at n. 23; *Zenith Radio Corp.* v. *Hazeltine Research, Inc.*, 401 U.S. 321, 331 (1971) (dictum). Curtis has failed to show any reason for disturbing the exercise of that discretion here. In view of Curtis' failure to raise the damages issue earlier, we hold that Judge Stewart's ruling was correct.

Finally, since it is abundantly clear that the assignment's "initial and first" language was unclear, parol evi-

dence was admissable. Such testimony came in not to contradict, add to or vary the written contract, but to aid in its understanding.

We affirm the judgment.

WILLIAM H. TIMBERS
United States Circuit Judge

THOMAS J. MESKILL
United States Circuit Judge

JOHN F. DOOLING, JR.
United States District Judge
Sitting by Designation

APPENDIX B

Opinion of the United States District Court for the Southern District of New York (November 30, 1976)

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

76 Civ. 1154

GOULD PAPER CORPORATION,
Plaintiff,

—against—

CURTIS CIRCULATION COMPANY,
Defendant.

MEMORANDUM

STEWART, District Judge:

In this action, plaintiff Gould Paper Corporation ("Gould") seeks to enforce against defendant Curtis Circulation Company ("Curtis") Gould's right to the payment of monies which it alleges Penthouse International Ltd. ("Penthouse") owes it for paper supplied by Gould to Penthouse. Gould alleges that Curtis is liable for payment by virtue of a security agreement in which Penthouse assigned to Gould the proceeds due to Penthouse under a distribution contract between Curtis and Pent-

house. Penthouse now seeks to intervene under Rule 24 of the Federal Rules of Civil Procedure ("F.R.Civ.P.") as a defendant.

Before considering the grounds asserted by Penthouse in support of its motion to intervene, we think it will be helpful to set forth exactly what issues are involved in this action.

Both Gould and Curtis recognize that there is an issue to be tried as to whether or not the assignment from Penthouse to Gould was released by Gould and is no longer valid (Pre-Trial Order ¶8). The assignment was collateral security for the amounts Penthouse became indebted to Gould for paper which Gould delivered to Penthouse pursuant to a contract between the two. The parties disagree as to whether there also exists an issue as to whether or not there is a debt owing from Penthouse to Gould to which this security agreement can attach (Pre-Trial Order ¶9).

The parties have stipulated that Penthouse received the January and February, 1976 deliveries of paper for which payment is sought and that the paper was received in good condition (Pre-Trial Order ¶4 (h) and (i)). There is no claim that the paper was not of good quality. Plaintiff argues that upon Gould's timely performance of its obligations under the contract, Penthouse became obligated to pay Gould the contract price for the two deliveries, and thus that a debt owing from Penthouse to Gould was created at this time.

Defendant contends that Penthouse never became obligated to pay Gould for the deliveries in issue here because Gould had overcharged Penthouse on prior paper shipments. In the state court action Penthouse has brought against Gould, Penthouse claims that these overcharges

amount to in excess of $2,000,000. In this same action, Penthouse has also sought $5,000,000 from Gould for damages to Penthouse's business reputation. In the instant action, defendant argues that because these Penthouse claims far exceed Gould's claim, there is no debt owing from Penthouse to Gould, and thus no debt to which the security agreement can attach.

We do not agree with defendant's reasoning. We find that a debt was created when Gould performed its obligations under the contract by making its January and February, 1976 deliveries which were accepted by Penthouse. That Penthouse may have set-off claims for overcharges and trade libel against Gould does not affect the original creation or continued existence of this debt. The existence of a set-off does not affect either party's right to sue or entitlement to a remedy, but simply means that there may be an adjustment of the amount ultimately recoverable as between the parties. 4 *A. Corbin, Contracts* §896 (1951).[1] Thus Penthouse's claims against Gould for overcharges and trade libel need not be litigated in order to determine whether there is a debt in existence between Penthouse and Gould to which the security interest could attach, and the outcome of this action can in no way prejudice these claims. The parties have stipulated to the facts which are necessary to establish this debt, namely Gould's timely delivery of the paper in good condition

[1] We do not think that Gould's alleged breach of the contract by overcharging is of such a nature as to be grounds for the complete discharge of Penthouse's obligations under the contract. See 5A *A. Corbin, Contracts* §§1228-1230 (1951); *Restatement of Contracts,* §§274-277 and §397 (1932); *Restatement in the Courts, Contracts* §§274-277, 397 (1965 Supp.).

Appendix B

and Penthouse's acceptance thereof. Accordingly, we find that the existence of the debt has been established in this action, and is not at issue here.

We can now consider Penthouse's motion to intervene in light of the single issue present in this action: whether there is a valid assignment still in existence between Gould and Penthouse of Penthouse's rights under its distribution agreement with Curtis.

Rule 24(a) states in pertinent part that intervention as of rights is appropriate where

> . . . the applicant claims an interest relating to the property or transaction which is the subject of the action and he is so situated that the disposition of the action may as a practical matter impair or impede his ability to protect that interest, unless the applicant's interest is adequately represented by existing parties.

Penthouse does have an interest in the proceeds of its distribution agreement with Curtis, and thus it has an interest in defeating the assignment. This interest is identical with that represented by defendant Curtis. *United States* v. *International Business Machines Corporation,* 62 F.R.D. 530 (S.D.N.Y. 1974). To protect this interest, Curtis has vigorously and thoroughly raised the defense that the assignment was terminated, presenting all the evidence which would be available to Penthouse on the issue. Further, Penthouse's attorneys have represented Curtis throughout the proceedings in this court. Thus we find that Penthouse's interest in the assignment is adequately represented by the existing parties, and intervention as of right is not appropriate. *IBM, supra; Carrol* v. *American Federation of Musicians of the United States and Canada,* 33 F.R.D. 353 (S.D.N.Y. 1963).

Appendix B

Rule 24(b) states in pertinent part that permissive intervention is appropriate where

> . . . an applicant's claims or defense and the main action have a question of law or fact in common. . . . In exercising its discretion, the court shall consider whether the intervention will unduly delay or prejudice the adjudication of the rights of the original parties.

In considering Penthouse's motion under this section, we note, first, that Penthouse's claims and defenses and the main action have common questions of law and fact only as to the single issue of the validity of the assignment. As to this issue, we have found that Penthouse's interest is adequately protected by the existing parties. As to all the claims which Penthouse has raised in its state court action, and which it seeks to assert by way of counterclaim in this action, should intervention be granted, there are no questions of law and fact in common with the main action. Rather, the state claims raise complex issues of law and fact which go far beyond the parameters of the instant litigation and appear to require substantial discovery before they are ready for trial. In May, after our denial of Gould's motion for a preliminary injunction, we found that Gould had shown the basis for an expedited trial on the merits. In light of this showing, we find that to permit Penthouse to intervene permissively and assert its counterclaims would unduly delay and prejudice the adjudication of the rights of the original parties. Thus we decline to exercise our discretion to allow Penthouse to intervene under Rule 24(b).

Appendix B

Accordingly, Penthouse's motion to intervene is denied in all respects.

So ordered.

(Illegible)
United States District Judge

Dated: New York, N.Y.
November 30, 1976.

APPENDIX C

Opinion of the United States District Court for the Southern District of New York (November 2, 1977)

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

76 Civ. 1154

GOULD PAPER CORPORATION,

Plaintiff,

—against—

CURTIS CIRCULATION COMPANY,

Defendant.

MEMORANDUM

Stewart, District Judge:

In this diversity action, plaintiff Gould Paper Company ("Gould") in two causes of action arising from the same transaction seeks injunctive relief and damages against defendant Curtis Circulation Company ("Curtis"). Gould's motion for a preliminary injunction was denied for failure to show possible irreparable harm after which plaintiff abandoned its cause of action for injunctive relief and the case went to trial before the Court without a jury on the cause of action seeking damages.

Appendix C

According to the stipulated facts, Gould entered into a contract with Penthouse International Ltd. ("Penthouse") on December 29, 1969 for the sale of paper to Penthouse. This agreement was superseded by a new contract, dated January 1, 1973 but not executed until July, 1973.

In April, 1969 Curtis entered into an agreement with Penthouse under which Curtis undertook to handle exclusively the newsstand distribution of Penthouse Magazine in the United States and Canada. This agreement was amended in August, 1971. Under the agreement as amended, Curtis is obligated to pay Penthouse each month a portion of the proceeds of the newsstand sales of Penthouse Magazine.

In August, 1969 Penthouse executed and delivered to Gould a written assignment ("Assignment") under which Penthouse assigned to Gould its right to the proceeds from its agreement with Curtis as security for the payments due to Gould for the sale of paper from Gould to Penthouse. The sole issue at the trial was whether this Assignment was still in effect or whether it had been released by Gould in 1972 in connection with the January 1, 1973 Gould-Penthouse agreement.[1] There is no writing which expressly release or terminates the Assignment.

In January and February, 1976, Gould shipped paper to Penthouse which was received in good condition. Penthouse has refused to pay for these shipments and Gould is here seeking to enforce the Assignment against Curtis for the amount of the payment due, which the parties have stipulated to be $717,786.33.[2]

[1] In a state court action by Penthouse against Gould, Penthouse claims overcharges by Gould in the sale of paper to Penthouse in excess of $2,000,000. Here, Curtis claims that because these claims far exceed Gould's claim, there is no debt owing from Penthouse to Gould and thus no debt to which the security agreement can attach. Curtis asserts therefore that this issue is also before the Court. In our pre-trial order of November 30, 1976, we held that this issue was not before the Court.

Appendix C

Since it is agreed by the parties that there is no document evidencing a release of the Assignment, defendant has the initial burden of overcoming a presumption in favor of the continued validity of the Assignment. The presumption loses force if evidence to the contrary appears. *Fleming* v. *Ponziani*, 24 N.Y.2d 105, 111 (1969); 9 Wigmore, Evidence § 2491 (1940). Under New York law the defendant must also show that cancellation of the Assignment was "clearly expressed", "unqualified and positive", "express and absolute" in order to sustain its affirmative defense. *Frank Associates* v. *John J. Ryan & Sons*, 281 App.Div. 665, 117 N.Y.S.2d 406 (1st Dept. 1952); *Associated Food Stores, Inc.* v. *Siegel*, 10 A.D.2d 1003, 205 N.Y.S.2d 208, 210 (2d Dept. 1960). In any event as indicated herein, we conclude that on all the evidence plaintiff has shown that the Assignment was not released.

When negotiations for a new agreement began in the spring of 1972, the situation of the parties had changed somewhat since the 1969 agreement was entered into. Penthouse Magazine, which was first published in this country in 1969, was now a successful publication, having achieved in three years a circulation of 3,000,000 copies. Consequently it needed an assured source of paper for a relatively long period. Penthouse, having become Gould's largest customer, also was in a stronger position (because

[2] Penthouse has agreed to indemnify Curtis against any loss in this action and Penthouse's lawyers have conducted the defense for Curtis.

of the volume of its purchases from Gould) to ask for better prices and better payment terms. And it could argue with some force that the Assignment should be released.

On the other hand, Gould had a substantial line of credit with major banks which it needed to retain in order to pay its supplying paper mills on a timely basis. From the onset of the relationship between Gould and Penthouse, the latter had consistently failed to make timely payments to Gould. Since Gould's line of credit was secured by its accounts receivable and since the Penthouse receivables were 20% of Gould's total accounts receivables and close to Gould's total net worth, the latter's bankers were understandably concerned about the security for and the delays in Penthouse's payments to Gould.

Plaintiff, who apparently initiated the negotiations for a new contract, was interested not only in obtaining a long-term contract (the 1969 agreement expired in 1974) but also in improving the timeliness of Penthouse's payments. The parties are agreed that during the negotiations Gould indicated a willingness to release the Assignment. Plaintiff contends that it made clear its willingness to do so was subject to a demonstration by Penthouse of its capability to make timely payments to Gould. Penthouse on the other hand contends that Gould's only condition was a release by Wisconsin Cuneo Press, Inc. ("Cuneo") of an assignment of certain newsstand and advertising proceeds of Penthouse.

The Cuneo assignment was indeed released and the release was confirmed in an exchange of letters between Cuneo and Penthouse in August-October, 1972. Although plaintiff agrees that release of the Cuneo assignment was a pre-condition to release of its own Assignment, Gould

contends that since the more essential condition—prompt payment by Penthouse—was never met, it was never willing to, and did not, release the Assignment. Set forth below are the reasons why we agree with plaintiff.

1. The testimony as to whether there was an oral agreement to release is conflicting.[3] Kreditor testified that he told Gould of the Cuneo release, that Gould said "Good", and that Kreditor interpreted this to mean that the Assignment could or would then be released. Billman testified that he told Lala of the Cuneo release and, although he could not remember what Lala then said, he understood the response as indicating the Assignment was released. Guccione testified that someone from plaintiff, he could not remember what person, pointed to the "entire agreement" clause of the new agreement as confirmation that the Assignment had been released.

Gould on the other hand testified that he would not release the Assignment until the payment record of Penthouse had been substantially improved, that his letter of August 7, 1973 (after the 1973 agreement had been executed) was an effort to work out an arrangement by which this could be accomplished, that he needed such improve-

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[3] On plaintiff's pre-trail motion for a preliminary injunction, defendant's principal witness at the hearing, Billman, testified that the Assignment was orally released by plaintiff in July, 19?? when the terms of the new contract between Gould and Penthouse were finally agreed to and the contract was executed. For various reasons, we found Billman's testimony not credible (see our Memorandum Opinion, May 19, 1976, denying the motion). In a Pre-Trial Order executed by the parties in October, 1976, defendant adhered to the position that the Assignment was released in July 1973. However, literally on the eve of trial in January 1977, the defendant served a Supplemental Pre-Trial Order asserting a new position, that is, the Assignment was orally released at some unspecified time in 1972.

ment before he could expect his bankers to continue the line of credit in the absence of the Assignment, that Penthouse never made any substantial improvement in the time of payments, and that accordingly he never released the Assignment. Lala's testimony was to the same effect.

Kreditor also testified that he had been told, perhaps by Billman, that plaintiff wanted to see a written confirmation of the Cuneo release. Billman testified that he showed the October 10, 1972 Cuneo letter to Lala, the letter according to Penthouse having been obtained specifically for the purpose of demonstrating in writing the Cuneo release. However, both Gould and Lala (although agreeing that the Cuneo release was a pre-condition of releasing the Assignment) deny that they asked to see any written confirmation or that they ever saw the October 10, 1972 letter until this lawsuit. Significantly, Billman asserted at the preliminary injunction hearing that he had never seen the October 10, 1972 letter.

The testimony of Kreditor, which we accept, to the effect that Gould said "Good" does not persuade us that Gould intended by that single word to indicate release. It seems more likely that he was only acknowledging that one precondition (the Cuneo release) to release of the Assignment had been met. The testimony of Billman even were we to assume that the inconsistencies between his testimony at trial and at the preliminary injunction hearing were innocent, does not lead us to reject the testimony of Lala. Nor does the testimony of Guccione, who was to say the least somewhat removed by his own choice from the negotiating arena and the commercial aspects of the enterprise, give us any reason to doubt the testimony of Gould.

Moreover, the letter of October 10, 1972 would appear to be the follow-up letter which Cuneo's earlier letter of

August 6, 1972 says will be forthcoming. And there is nothing on the face of the October 10, 1972 letter which suggests that it was prepared to enable Penthouse to use it to confirm to Gould the Cuneo release.

The August 7, 1973 letter from Gould to Kreditor is also on its face fully consistent with plaintiff's position that any release of the Assignment would be in a subsequent "side letter". It proposes a program under which Penthouse could become substantially more current in payment and which, if complied with (and it was not) would meet plaintiff's conditions for releasing the Assignment.

Throughout the testimony of Kreditor, we received the clear impression, from his statements, from the care which he obviously took to answer questions as accurately and precisely as possible and from his demeanor in the courtroom, that he is a man who (as he puts it) likes to dot every "i" and cross every "t". We find it difficult to accept that Kreditor, who testified that no contract was entered into by Penthouse without his prior approval, would have failed to demand and obtain a written release at or before the execution of the 1973 agreement.

It may be that Penthouse believed the Assignment had been orally released; certainly, plaintiff did not. We can find nothing in the latter's conduct which can reasonably be said to have been engaged in for the purpose of misleading Penthouse in this respect. Nor can we find that plaintiff took any action which amounted to an agreement to release the Assignment.

2. Penthouse points to the "entire agreement" clause in the 1973 agreement, which is exactly the same as a clause in the 1969 agreement, as evidence that the Assignment had been released. The Assignment was executed four

months before the 1969 agreement but no suggestion was made by Penthouse that the latter terminated the Assignment. There is, as we initially found in our Memorandum of May 19, 1976, still no credible evidence to support Penthouse's contention that this "boilerplate" was intended by the parties as an indication that the Assignment had been released.

3. The Assignment was of significant importance to Gould and its release would have been of at least equal importance to Penthouse. It is surely significant therefore, that there is no writing embodying or confirming the asserted release. A personal assignment by Guccione, Chairman of Penthouse, which was entered into at the same time as the Assignment and secured the same obligation, was released in 1971 in writing. The release of the Cuneo assignment was confirmed in writing. The Assignment remains in Gould's possession; its return has never been requested by Penthouse.

4. Penthouse had reasons of its own for seeking release of the Cuneo assignment. Like any security obligation, Penthouse found it a burden. Unlike the Assignment, it covered advertising as well as newsstand revenues. Penthouse had independently and unsuccessfully sought its release in 1971. Moreover, the release involved a cash pre-payment by Penthouse to Cuneo of $700,000. No similar payment was made by Penthouse to Gould at the time defendant says the Assignment was released. Although Gould made it clear that it would not even consider releasing its Assignment unless Cuneo had released its assignment, the fact that the latter happened is not persuasive evidence that the Assignment was released by Gould.

5. Penthouse relies on the undisputed evidence that a footnote in its financials referring to the Assignment and

the Cuneo assignment did not appear in the 1972 financials or thereafter Gould had copies of these financials and reviewed them. It appears that, commencing with the 1972 financials, the Penthouse audits were prepared by an accountant different from the one who prepared the earlier audits. It also appears that the new accountant, in dropping the footnote, checked sources which would have been unable to confirm whether or not (as he had been advised by Penthouse) the Assignment had been in fact released and he did not seek confirmation from Gould. In any event, it is clear that after the 1972 and 1973 financials were published, Gould continued to assert to its bankers that the Assignment had not been released.

6. Curtis customarily sent two checks to Penthouse each month, one made out to Penthouse and one to Gould. The latter was then delivered to Gould by Penthouse. The amounts were determined by Penthouse and given to Curtis in advance. Prior to November, 1972, the amounts on neither check were rounded. Commencing in that month, the amounts on the check payable to Gould were always in round figures. Two checks were prepared each month, except on six occasions, until April, 1975. Thereafter, only one check which was payable to Penthouse was prepared.

Penthouse contends that the shift to round figures in November 1972 demonstrates that the Assignment had been orally released at some unspecified date theretofore. This contention is squarely inconsistent with Billman's prior testimony that the rounding did not begin until the Assignment had been released, that is, in July 1973. At trial

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[4] The financials for each year were issued in September or October of the following year. By the time the 1972 financials were published the Cuneo assignment had, of course, been released.

Billman conceded he was in error and that he now recalls the rounded payments began in November 1972 following the release of the Assignment. In any event, the facts are that Curtis was under no obligation to make any monthly payments to Gould since the Assignment was only a security instrument, the payments by two separate monthly checks continued without interruption for a long period after November 1972, and Gould's only interest was in being paid, not by whom. We cannot find therefore that the rounding which began in November 1972 indicates anything other than that Penthouse may have thought that the Assignment had been released (if, indeed, even that), and not that it had indeed been released.

7. Defendant contends that Gould's failure to assert the Assignment in 1973-1975, at times when it assertedly needed cash, confirms the fact of the release. However, there is no convincing evidence that Gould had ever asserted the Assignment prior thereto; the letters upon which defendant relies (Exhs. G, H, 20A, 20B) can hardly be said to be demands for payments in default or threats to enforce the Assignment. Moreover, it seems clear that Penthouse on several occasions in 1973-1975 reassured Gould that its late payments would be forthcoming shortly and, that in the interests of harmony, Gould may well have decided not to assert its security instrument. During this same period also, Gould from time to time reassured its bankers that the Assignment remained in effect. And in May 1975, Gould drafted a letter to defendant to enforce the Assignment. The letter was not sent at that time; it was eventually sent in February 1976 and this action followed soon thereafter. We cannot find therefore, that the evidence of plaintiff's conduct after the alleged release confirms its existence.

For the foregoing reasons and on all the evidence, we find that the Assignment was not released. Accordingly, plaintiff is entitled to judgment in the amount of $717,786.33 with interest and costs.

Settle order on two days' notice.

So ordered.

(Illegible)
United States District Judge

Dated: New York, New York
November 2, 1977.

APPENDIX D

Opinion of the United States District Court for the Southern District of New York (June 15, 1978)

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

76 Civ. 1154

GOULD PAPER CORPORATION,

Plaintiff,

—against—

CURTIS CIRCULATION COMPANY,

Defendant.

STEWART, District Judge:

Following trial in this case last year, we issued our opinion dated November 2, 1977 holding that the Assignment, dated August, 1969, had not been released by plaintiff in 1972 and that it continued in effect thereafter. It was our view at the time that the question of whether or not the Assignment had been released was the only issue to be decided (Memorandum Opinion, p. 2). The pre-trial order described the sole issue to be tried as follows: "was the Assignment still in full force and effect?" The evidence offered at trial by the parties was also consistent with this description of the issue before the Court.

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When we asked the parties to settle an order, however, defendant disagreed with plaintiff as to the amount of damages. The parties had stipulated that defendant owed plaintiff $717,786.33 for paper shipped by plaintiff to Penthouse for use in the March, April and May, 1976 issues of Penthouse Magazine and it had been our view (and apparently plaintiff's view) that this was the amount in dispute. Defendant contended, however, that only a portion of this amount was covered by the Assignment and was recoverable in the judgment.

The Distribution Agreement between Gould and Curtis, dated April 3, 1969, provided that Curtis would make three payments to Penthouse from the proceeds of the sale of each issue of the magazine distributed by Curtis, as follows:

(1) "Curtis will pay Publisher [Penthouse] on the on-sale date" a stated percentage of the estimated proceeds;

(2) "A second payment, if any, . . . will be made by Curtis to Publisher as shall be necessary to provide settlement for ninety percent (90%) of the estimated net sale sixty days (60) after off-sale date";

(3) "A third payment, if necessary, for 100% of the then estimated net sale will be made to Publisher 180 days after off-sale date".

The Assignment states in relevant part:

". . . in order to secure Gould Paper Corporation the payment of monies now due and to become due, the said Penthouse International, Ltd., hereby sells,

assigns and transfers, and by these presents does sell, assign and transfer to Gould Paper Corporation, all of its right, title and interest in and to the proceeds of a certain distribution contract with Curtis Circulation Company of 641 Lexington Avenue, New York, New York, dated April 3rd, 1969, a copy of which is annexed hereto and made a part hereof,* see rider[1] it being understood and agreed that this assignment shall attach to the initial and first payments to be made thereunder."

Defendant argues that pursuant to the last clause which refers to "the initial and first payments", the Assignment applies only to the payment on the "on-sale date" (estimated to be 50% of the total sale). Defendant also argues that this clause is intended to limit the preceding language which refers to an assignment of "all of its [Penthouse's] right, title and interest in and to the proceeds of" the Curtis Distribution Agreement. Thus, if the rider is interpreted literally (as defendant says it should be), when plaintiff invoked the Assignment on February 23, 1976, it was applicable only to about $80,000 of proceeds received by Penthouse under the Distribution Agreement. Plaintiffs contends that the Assignment was not limited to the "on-sale date" payment and applies to all of the payments due for each issue; accordingly, plaintiff contends that the Assignment applies to $717,786.33 of proceeds.

[1] The rider, which is physically attached to the Assignment, reads:

* it being the intent of the parties to limit the aforementioned assignment to the bills owed to the Assignee on an issue by issue basis, as follows:

That the proceeds of the prior month's issue shall be applied only to the paper bills for the following month's issue.

Since we have found that there was a clear misunderstanding as to the issues before the Court, in which we shared, and that the issue of the scope of the Assignment should properly be presented to the Court, we held further hearings to decide this question.

At the supplemental hearings, plaintiff presented the testimony of Peter Gould and Jerry Mutchnick, two of its officers who negotiated the Assignment on behalf of Gould, and Paul Gloe, a former officer of Cuneo Press.[2] Defendant offered the testimony of Robert Guccione, Chairman of Penthouse. The negotiation of the Assignment began in 1968 and continued until its execution in August, 1969. At the time, Penthouse had almost no assets in this country; the magazine had commenced publication in England and almost all of its assets were located there. When Penthouse asked Gould to supply paper for its new venture into the publication of the magazine in this country, Gould insisted on substantial security which would be available in this country. It eventually obtained the Assignment here in question, as well as security agreements from Guccione and from the British Penthouse company.

Peter Gould and Mutchnick each testified that throughout the neogtiations it was made clear to Ernest that plaintiff would require an assignment of the entire proceeds of newsstand sales and it was their testimony that from the outset Ernest on behalf of Penthouse agreed to this. They further testified that, Guccione (who apparently attended only two of the several meetings on the Assignment) attended a meeting in January or February, 1969, and confirmed that Gould would have an unlimited assignment of the proceeds of newsstand sales.

[2] Dominick Lala, another Gould officer, also testified briefly.

Appendix D

Subsequently, after the Distribution Agreement had been signed, Peter Gould and Mutchnick again met with Ernest who advised them that Cuneo Press would be the printer and that it also wanted an assignment of the Distribution Agreement, similar to that obtained by Gould. Peter Gould told Ernest this was unacceptable and Ernest then suggested that Peter Gould try to work out an acceptable arrangement with Cuneo. The latter thereupon got in touch with Paul Gloe at Cuneo and the two agreed that Gould had first call on all newsstand receipts and Cuneo, after Gould had been paid, would have a second call. Peter Gould reported this agreement to Ernest who did not object.

The Penthouse assignment to Cuneo, dated June 23, 1969, provided that Cuneo should have:

> "II A secondary assignment of newsstand receipts, second only to Gould Paper Co."

This agreement supplemented a Wisconsin Cuneo Press proposal dated June 20, 1969 (and accepted by Penthouse sometime prior to July 14, 1969 when it was approved by Wisconsin Cuneo) which provided in part:

> "Customer's Property: It is understood that the printer may retain possession of all art work, plates, cuts, negatives, positives, paper, partially completed and completed work, and any other material belonging to customer, and shall also have a lien upon goodwill, copyrights, subscription lists, trade marks and tradenames, appertaining to customer's work or security for payment of its bills. If customer defaults for three months in payment of bills for work other than for periodical publications, or for three days in payment for periodical publications or other publications designed for sale at a specific time, the printer may dispose of all customer's property as waste material or as literary material, as in printer's sole discretion it deems best, without notice to or demand on the customer, crediting proceeds, less reasonable expenses of sale, or indebtedness."

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Gloe was recruited by John Cuneo in connection with the impending arrangements by Cuneo Press to print Penthouse magazine. He was initially employed in 1969 as a Vice-President of Cuneo Press and general manager of the Wisconsin Cuneo Press division.[3] Gloe testified that he began work before the Cuneo-Penthouse agreements were executed; that he always understood that Cuneo's position as an assignee of the proceeds under the Curtis agreement was second to Gould as to all payments by Curtis to Penthouse, not just as to the "on-sale date" payments; and that John Cuneo relied principally on the Penthouse assignment of advertising receipts for security.[4] Pursuant to the provision on "Customer's Prop-

[3] His employment at Cuneo terminated in February, 1972.

[4] Guccione's forecasts for the proceeds of newsstand sales to be obtained from Curtis indicated that they would be more than sufficient to pay both Gould and Cuneo. It was also expected, accurately as events demonstrated, that Gould's bills would be approximately the same as Cuneo's. Thus, Cuneo could reasonably expect that, even after Gould had been paid for a particular issue, there would be proceeds available to cover Cuneo's bills for that same issue. It seems arguable, therefore, that Cuneo would have been quite content with a second assignment after Gould of all newsstand receipts, especially in view of its security rights in advertising revenues and in the paper to be received from Gould.

erty", *supra*. Cuneo also had a lien on the goodwill, copyrights, subscription lists and trade marks of Penthouse, as well as a right to all of the Gould paper shipped to Cuneo each month. Gloe also confirmed Peter Gould's testimony that the latter called Gloe early in the summer of 1969 to determine the Gloe's understanding of the security arrangements. Gloe testified that he advised Peter Gould he understood the arrangement to be that Gould had a "first call" on all the newsstand receipts, Cuneo had an assignment on the advertising receipts and had a second assignment after Gould on all newsstand receipts. Gloe also testified that he had been so advised by Ernest. We found Gloe's testimony to be thoroughly credible in every respect.

The Assignment was drafted by John Crowe (now deceased), a lawyer for the Paper Merchants Association. Mutchnick, at Peter Gould's direction, asked Crowe to prepare a draft of the document and instructed Crowe to provide in the Assignment that Gould was "to come first before anyone" as to proceeds under the Curtis Distribution Agreement. At this time, Gould knew that Penthouse was negotiating with Cuneo and that the latter was seeking an assignment from Penthouse as security. Crowe sent the draft to Gould by letter dated June 4, 1969. This, the first draft of the Assignment, is in all material respects the same as the document finally executed by Penthouse in August, 1969, except for the addition of the rider.

Guccione testified that he insisted the word "initial" be added to an early draft in order to insure that the words "first payments" meant first payments, that is, the "on-sale date" payment. We think Guccione is mistaken in his recollection and that the words "initial" and "first payments" were placed in the draft by Crowe in accordance with Gould's instructions to ensure Gould had an assign-

ment to all the Curtis proceeds prior to anyone else, including in particular Cuneo. In this connection, we note that the Distribution Agreement does not refer anywhere to a first payment but uses the words "on-sale date" to describe the first payment, a phrase which does not appear in the Assignment. Crowe had been furnished the Distribution Agreement (which is specifically referred to in the Assignment) and, as was also the case with Guccione, could have used the precise language in that agreement, that is, "on-sale date", if he had intended to refer only to that payment. The use of other language is, we think, significant. We conclude that the Assignment encompassed each of the payments to be made by Curtis to Penthouse on each issue of the magazine.

Guccione also attended a meeting in late August, 1969, at which he insisted that a clause be inserted in the Assignment to ensure that the Assignment be limited to an issue-by-issue basis.[5] Gould agreed to this; Guccione drafted the rider and it was added to the Assignment which was then executed. Plaintiff contends that the testimony demonstrates the rider was understood by the parties as providing the opposite of its literal language, that is, that the parties understood it to mean that the proceeds of the following month's issue should be applied to the paper bills for the preceding month's issue. Defendant argues on the other hand that the language itself, the meaning of which is not in dispute, controls. Since we understand that, in light of our conclusions as to the meaning of "initial" and "first payments", it is unnecessary for us to decide this question, we do not reach it.

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[5] Incidentally, if the Assignment had been intended to cover only the "on-sale date" payment, there would have been no need to spell out in the rider that the Assignment would be limited to an issue-by-issue basis.

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Accordingly, we affirm our conclusion that plaintiff is entitled to judgment in the amount of $717,786.33 with interest and costs.

Settle order on two days' notice.

So ORDERED.

CHARLES ETHRATZ
United States District Judge

DATED: New York, New York
June 15, 1978.

APPENDIX E

Assignment from Penthouse International, Ltd. to Gould Paper Corporation dated August 1969

KNOW ALL MEN BY THESE PRESENTS, THAT:

Penthouse International, Ltd., having its principal place of business at 110 East 59th Street, City, County and State of New York, in consideration of the sum of One ($1.00) Dollar to it in hand paid by Gould Paper Corporation, a New York corporation, having its principal office for the transaction of business at 145 East 32nd Street, City, County and State of New York, and in consideration of the acceptance by Gould Paper Corporation of purchase orders for a quantity of paper, and in order to secure Gould Paper Corporation the payment of monies now due and to become due, the said Penthouse International, Ltd., hereby sells, assigns and transfers, and by these presents does sell, assign and transfer to Gould Paper Corporation, all of its right, title and interest in and to the proceeds of a certain distribution contract with Curtis Circulation Company of 641 Lexington Avenue, New York, New York, dated April 3rd, 1969, a copy of which is annexed hereto and made a part hereof,* it being understood and agreed that this assignment shall attach to the initial and first payments to be made thereunder.

That as a further inducement to Gould Paper Corporation to accept the assignment of the proceeds of said distribution contract, and to make delivery of the paper required to complete the manufacture of the magazines so

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* [Rider] it being the intent of the parties to limit the aforementioned assignment to the bills owed to the Assignee on an issue by issue basis, as follows:

> That the proceeds of the prior month's issue shall be applied only to the paper bills for the following month's issue.

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identified in said contract of distribution, and to accept as security for monies due and to become due, Penthouse International, Ltd., represents and warrants:

1. That the contract with Curtis Circulation Company, a copy of which is annexed hereto, is a good and valid contract in every respect, free of and from any defenses or claims of whatsoever nature, and that said contract has not been cancelled, withdrawn or modified in any respect, and that said contract has not been otherwise assigned or encumbered.

2. In the event the monies received by Gould Paper Corporation under this assignment are insufficient to pay all monies now due and to become due from Penthouse International, Ltd., and/or Penthouse Publications, Ltd., of London, England, the guarantor of obligations of Penthouse International Ltd., for merchandise delivered or contracted for, then and in such event, Penthouse International, Ltd., agrees to pay to Gould Paper Corporation any deficit or deficiency promptly upon demand.

IN WITNESS WHEREOF, Penthouse International Ltd., has caused this instrument to be executed by its duly authorized officer and its corporate seal affixed this day of August, 1969.

PENTHOUSE INTERNATIONAL, LTD.

By: (ILLEGIBLE)

(Corp. Seal)

Appendix E

STATE OF NEW YORK }
COUNTY OF NEW YORK } ss.:

On this 28th day of August, 1969, before me personally came Robert Guccione, to me known, who being by me duly sworn did depose and say: that he resides at ; that he is the President of Penthouse International, Ltd., the corporation described in and which executed the foregoing instrument; that he knows the corporate seal of said corporation; that the seal affixed to said instrument is such corporate seal; that it was so affixed by order of the Board of Directors of said corporation and that he signed his name thereto by like order.

IRVING S. KLEIN
Notary Public State of New York
No. 31-7293500
Qualified in Queens County
Certificate Filed in New York County
Commission Expires March 30, 1970

IN THE

Supreme Court of the United States

October Term, 1978

No. 78-1208

CURTIS CIRCULATION COMPANY,

Petitioner,

against

GOULD PAPER CORPORATION,

Respondent.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Second Circuit

RESPONDENT'S BRIEF IN OPPOSITION

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February 7, 1979

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RESPONDENT'S BRIEF IN OPPOSITION

The respondent, Gould Paper Corporation, respectfully requests that this Court deny the petition for a writ of certiorari to review the unanimous *per curiam* decision of the United States Court of Appeals for the Second Circuit entered on December 13, 1978.

Questions Presented

1. Whether the District Court and the Court of Appeals erred in applying the clear mandate of Section 9-318 of the Uniform Commercial Code to bar an account debtor under an assignment from raising against the assignee personal claims of the assignor unrelated either to the creation of the debt between the assignor and the assignee or to the account between the debtor and the assignor?

2. Whether the District Court abused its discretion when, following its decision on the sole issue submitted for trial under the Pre-Trial Order, it received additional

evidence relating to an alleged limitation on damages which was first articulated by the defendant after trial?

Statutes Involved

This case involves the following statute in addition to the one quoted in the petition:

N.Y. U.C.C. §9-204, which provides in part:

> "(1) A security interest cannot attach until there is agreement (subsection (3) of Section 1-201) that it attach and value is given and the debtor has rights in the collateral. It attaches as soon as all of the events in the preceding sentence have taken place unless explicit agreement postpones the time of attaching."

Statement of the Case

The petition in this case raises no issue worthy of review by this Court. The first question presented involves purely state commercial law, on which the decisions of the courts below are well supported by New York statutory and common law. The second question seeks further review by this Court of a simple exercise of discretion by the District Court, unanimously affirmed by the Court of Appeals, which found the contention so lacking in merit as to "warrant only brief mention" in its *per curiam* opinion (3a).*

This commercial litigation arises from the wrongful refusal of petitioner to honor a written assignment. Gould Paper Corporation ("Gould"), the assignee, is a paper merchant. It purchases paper from mills and sells it directly to customers such as magazine publishers. Curtis Circulation Company ("Curtis"), the obligor under the assignment, is a nationwide distributor of magazines including *Penthouse* magazine, published by the assignor, Penthouse International Limited ("Penthouse"). The

* Citations of numbers followed by "a" are to pages of the appendix attached to the petition.

assignment ("Assignment") was negotiated by Gould in 1969 to protect it against the non-payment by Penthouse of its paper bills, by allowing Gould to look to Curtis. When Penthouse refused to pay Gould for more than $750,000 worth of paper shipped in January and February 1976, Gould sought to exercise its bargained-for security. However, Curtis, indemnified by Penthouse and represented by Penthouse's attorneys, refused to honor the Assignment, thus precipitating the instant litigation.*

In January 1977, the case was called for trial. The sole issue raised at trial—indeed the only defense specified in the Pre-Trial Order and in Curtis' post-trial brief—was Curtis' claim that the Assignment had been cancelled by Gould sometime after 1972. By decision dated November 2, 1977, the trial court rejected the testimony of the Curtis and Penthouse witnesses, found for Gould and awarded it $717,786.33—the amount stipulated by the parties as the value of the paper shipped to Penthouse in 1976 (Appendix C). Eight days later, Curtis wrote to Judge Stewart, demanding that the judgment be reduced to $88,720.80. For the first time in the litigation, Curtis argued that Gould's damages under the Assignment were limited by certain language in the Assignment—subsequently found by both the trial court and the Second Circuit to be unclear or ambiguous (2a, 3a). In light of Curtis' belated argument as to damages, Judge Stewart exercised his discretion to reopen the record for receipt of additional evidence on this defense.

The reopened trial began on March 20, 1978. After hearing all of the evidence, by its opinion of June 15, 1978

* Penthouse's only excuse for non-payment has been its still unproven claim that Gould "overcharged" Penthouse on *prior* unrelated shipments of paper going back to 1974. This "overcharge" claim was asserted against Gould by Penthouse in a New York state court action over three years ago but has yet to be tried. Gould has asserted counterclaims against Penthouse arising out of contractual disputes between them, for an amount in excess of these alleged overcharges.

(22a-30a), the District Court rejected Curtis' new defense that the language "initial and first payments" was meant to limit the Assignment and entered judgment for Gould on June 21, 1978.

In a unanimous *per curiam* decision entered only hours after oral argument on December 13, 1978, the United States Court of Appeals for the Second Circuit affirmed the judgment of the District Court substantially on the opinions below (Appendix A). The Court of Appeals held to be "without merit" petitioner's claim that Curtis should have been permitted to assert Penthouse's overcharges against Gould. The Court ruled that the clear language of New York's Uniform Commercial Code (§9-318) specifically sets forth the defenses available to an account debtor and does not include those of the assignor against the assignee. The decision to reopen the record to receive evidence on Curtis' belated defense was held to be one "committed to the discretion of the trial judge" and the Second Circuit found that Curtis had "failed to show any reason for disturbing the exercise of that discretion here," particularly since Curtis had failed to raise the damage issue during trial (3a).

Reasons for Denying the Writ

I

The courts below properly construed New York law.

The first issue raised by petitioner simply challenges the District Court's and the Court of Appeals' application of New York State commercial law. Curtis contends that, as account debtor, it should have been permitted to defeat the Assignment by asserting Penthouse's personal claims against Gould for alleged "overcharges" on earlier shipments of paper unrelated to the 1976 paper bills upon which Gould sued. There has never been any question that this

issue is governed solely by New York law, including the Uniform Commercial Code, which both courts below applied without great difficulty to bar Curtis from asserting the personal claims of Penthouse.

Rarely, if ever, does this Court grant review of such federal court determinations of state law, save in "exceptional cases." See, *Huddleston* v. *Dwyer*, 322 U.S. 232, 237 (1944); R. Stern & E. Gressman, *Supreme Court Practice*, 283 (5th ed. 1978). Here, far from showing anything exceptional, petitioner argues that the Second Circuit's *per curiam* decision *may* have some precedential value simply because it applies the Uniform Comemrcial Code, which is law in 51 jurisdictions. But petitioner shows absolutely no conflict among the states or the Circuit Courts of Appeals over the U.C.C. provisions involved in this case. Nor does it show that the decisions below are inconsistent with any decisions of this Court or with any state court interpretation of the relevant U.C.C. provisions. Rather, its argument is that this Court should review routine applications of state commercial law by the federal appellate courts merely because they are based on the U.C.C. —a proposition which, if accepted, would vastly expand this Court's already crowded docket.

There is absolutely nothing "exceptional" about the state law issue in this case. Although petitioner claims that the decisions below conflict with New York common law, it cites no authority holding that an account debtor may assert against the assignee the personal claims of the assignor. Rather, the decisions below are completely in accord not only with the specific language of New York's Uniform Commercial Code, but also with pre-existing common law. For this reason, petitioner's first contention is, as the Court of Appeals held, "without merit."

New York U.C.C. §9-318, sets forth the catalog of defenses available to an account debtor in a suit by an assignee:

> "(a) all terms of the contract between the account debtor and the assignor and any defense or claim arising therefrom; and
>
> "(b) any other defense or claim of the account debtor against the assignor which accrues before the account debtor receives notification of the assignment."

Precisely the same defenses, and no others, were available to the account debtor under common law prior to adoption of the U.C.C. 4 A. Corbin, *Contracts*, §896, at 595 (1961); *Restatement of Contracts*, §161 (1932). As the Second Circuit held (3a), the defense which petitioner was barred from asserting against Gould—namely Penthouse's claim of overcharges on unrelated sales of paper—is not among the defenses available to the account debtor. Only those defenses which the account debtor (Curtis) had against the assignor (Penthouse) or which the account debtor has *independently* against the assignee (Gould) can be asserted to defeat the enforcement of the Assignment.

In the face of the clear statutory framework of Section 9-318, and contrary to the "expressio unius" maxim, petitioner argues that since the defense it seeks to assert is not among those listed in U.C.C. §9-318, common law and not the U.C.C. must apply. But even if that strained reading of U.C.C. §9-318 had any merit, it would not help petitioner since, as noted, the defenses available to an account debtor under common law were exactly the same as those specified by the code.

As the Second Circuit held, the only authority cited by petitioner in seeking to show that common law was inconsistent with U.C.C. §9-318, *Warren* v. *Chemical Bank and Trust Co.*, 274 A.D. 785, 79 N.Y.S.2d 776 (1st Dep't 1948), is simply "not on point" (3a). In *Warren*, the condition precedent to creation of an obligation never occurred and thus no debt ever arose to which the security interest could attach.* *Warren* would be analogous if, but only if, Gould had not shipped paper to Penthouse in 1976, or if that paper had been defective. But here, it was stipulated in the Pre-Trial Order that paper was shipped and received in good condition. When the paper was received, the Assignment attached. Nothing in *Warren* suggests otherwise.

Petitioner seeks to avoid the force of U.C.C. §9-318 and the consistent common-law doctrine by arguing that they apply only to *absolute* assignments, not security devices, such as this Assignment was. But Article 9 of the Uniform Commercial Code (including both Sections 9-204 and 9-318) is by definition applicable to *secured* transactions, and both Corbin and the Restatement make absolutely no distinction between absolute and conditional assignments in discussing the defenses available to the account debter. Indeed, as Professor Gilmore noted in his treatise, *Security Interests in Personal Property*, §41.2 at 1082 (1965):

> "Defenses which may be asserted against an assignee whose right was originally subject to a condition are, apart from the condition itself, exactly the same as those which may be asserted against the assignee whose right was not conditional."

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* New York U.C.C. §9-204 states three conditions precedent to the creation of an enforceable security interest: (1) there must be an agreement that it attach; (2) value must be given; and (3) the debtor must have rights in the collateral. As the courts below held, all three conditions were met here—there was an agreement, the Assignment; value in the amount of $717,786.33 was given when the paper was shipped in January and February 1976; and Penthouse obtained rights in the proceeds of its Distribution Agreement with Curtis for the March, April and May issues of the magazine.

As noted in P. Cogan, W. Hogan & D. Vagts, *Secured Transactions Under the Uniform Commercial Code* (Bender's U.C.C. Commentary, Vol. 1A), §21.02, page 2175 (1978), once the assignment attached, the right to payment was unconditional, subject *only* to adjustments of the type allowed under U.C.C. §9-318(1).

In *Warren*, by contrast, the security interest never attached because no value was ever given.

Here, the only condition was the shipment of paper and it was stipulated that this condition was met. Accordingly, the Assignment was enforceable against Curtis, subject only to the defenses enumerated in U.C.C. §9-318, precisely as the Court of Appeals held.

II

The decision below properly affirmed the trial court's exercise of discretion.

As the Court of Appeals held, the second question presented in the petition warrants only brief mention (3a). The petition itself acknowledges (p. 8) that Judge Stewart's decision to reopen the record was an "exercise of discretion" and petitioner offers nothing which would justify review of that exercise by this Court.

This Court recognized in *Zenith Radio Corp.* v. *Hazeltine Research, Inc.*, 401 U.S. 321, 331 (1971) that "a motion to reopen to submit additional proof is addressed to [the trial judge's] sound discretion." The petition cites not a single case in which this Court, or even a federal Court of Appeals, reversed a trial judge's decision to reopen a record. As Professor Moore has stated, review of such a decision is extremely narrow and is subject to reversal "only in a rare case where abuse is clearly shown." 6A J. Moore, *Federal Practice*, §59.04 [13] (1974).

Upon reviewing the record in this case, the Court of Appeals not only failed to find an abuse of discretion, but held that:

> "[I]n view of Curtis's failure to raise the damages issue earlier . . . Judge Stewart's ruling was correct." (3a)

That the decision of the District Court was a proper exercise of discretion is clear from the facts. In January 1977, when the case was called for trial, the sole issue litigated was Curtis' defense that Gould had released the Assignment in 1973. This was the only defense specified in the Pre-Trial Order or advanced by Curtis in its post-trial brief. Not until after the trial ended and a final decision was rendered on what Curtis' own post-trial brief called "the sole issue before the Court" did Curtis raise the contention that Gould's damages, which had theretofore not been questioned, should be limited under its view of the scope of the Assignment.

Despite his understanding that the "sole issue" before the Court at trial was the release of the Assignment (22a), Judge Stewart nonetheless agreed to reopen the record, not to enable Gould to cure any "deficiency" in the evidence as to the amount of its damages—which had already been set forth in the Pre-Trial Order and at trial—but so that *Curtis* could introduce evidence on *its* belated contention that the Assignment was limited in scope. It is this decision *in its favor* that petitioner now challenges. Reopening of the trial under such circumstances cannot possibly have prejudiced Curtis, since once the trial was reopened, Curtis was given every opportunity to present evidence in support of its contention.

Petitioner rejects Judge Stewart's statement that both he and Gould believed the alleged release of the Assignment to be the sole issue at trial, based only upon a single brief colloquy on the opening day of a four-day trial in January 1977 (Petition, pp. 8-9). That colloquy shows only that Gould's counsel did *not* understand there to be any other issue before the Court. As Gould's counsel stated, he was "not sure what point Mr. Grutman intends to draw from that" and did not "know whether it was going to have any relevance." The colloquy only points up what the Court of Appeals found—that Curtis "fail[ed]

to raise the damages issue'' until November 1977, after it had lost on the only issue which was submitted for trial.

This Court need go no further than the cases cited by petitioner to recognize the full range of discretion afforded a trial judge in determining whether to reopen a record. As noted, not one represents a reversal by an appellate court of a trial judge's exercise of discretion. Indeed, in *Pacific Indemnity Co.* v. *Broward County,* 465 F.2d 99 (5th Cir. 1972) cited by petitioner (Petition, p. 10), the Court specifically held that once the need for additional proof on an issue not in the Pre-Trial Order became clear, the trial court ''could have ordered a limited new trial under Rule 59 F. R. Civ. P. where . . . the issue was in good faith overlooked by all concerned'' (465 F.2d at 104). That is precisely what the District Court did here and there is no reason for this Court to review that exercise of discretion after its unanimous affirmance by the Second Circuit.

Conclusion

For these reasons, the petition for a writ of certiorari should be denied.

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Respectfully submitted,

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